

MINUTES

MONTANA SENATE 57th LEGISLATURE - REGULAR SESSION COMMITTEE ON TAXATION

Call to Order: By **CHAIRMAN BOB DEPRATU**, on January 23, 2001 at 8:00 A.M., in Room 405 Capitol.

ROLL CALL

Members Present:

Sen. Bob DePratu, Chairman (R)
Sen. Alvin Ellis Jr., Vice Chairman (R)
Sen. John C. Bohlinger (R)
Sen. Mack Cole (R)
Sen. Pete Ekegren (R)
Sen. Jon Ellingson (D)
Sen. Bill Glaser (R)
Sen. Dan Harrington (D)
Sen. Emily Stonington (D)

Members Excused: None.

Members Absent: None.

Staff Present: Lee Heiman, Legislative Branch
Deb Thompson, Committee Secretary

Please Note: These are summary minutes. Testimony and discussion are paraphrased and condensed.

Committee Business Summary:

Hearing(s) & Date(s) Posted: Senate Bill 173, 1/12/2001
Executive Action: Senate Bill 2, Pass 9-0

HEARING ON SENATE BILL 173

Sponsor: SENATOR ALVIN ELLIS, SD 12, Red Lodge

Proponents: Webb Brown, Montana Chamber of Commerce

Opponents: Ken Nordtvedt, former Legislator and former Revenue Director; Betty Beverly, Montana Senior Citizens; Don Judge, AFL-CIO

Opening Statement by Sponsor: SENATOR ELLIS presented a written statement explaining SB 173. **EXHIBIT(tas18a01)** He said amendments were needed.

Proponents' Testimony: Webb Brown, representing the Montana Chamber of Commerce, spoke in support of the bill. He pointed out there were aspects of the income tax laws that discouraged people from moving to Montana, which has one of the highest marginal tax rates. **{Tape : 1; Side : A; Approx. Time Counter : 14 - 17.6}**

Opponents' Testimony: Ken Nordtvedt, former Legislator and former Revenue Director, and Vice Chairman for Montanan's for Better Government said this bill seemed like a big effort to accomplish little since it only changed the surface image of the marginal tax rate. He said nominally the change was the top rate from 11% to 6.6%, but because of the loss of deductibility of the federal income tax it was effectively a 6.8%-6.6% reduction in the effective rates on the highest income brackets in the state. This would mean a 3% reduction in the lower brackets in the effective tax rate, but this was in doubt. The bill basically increases income tax collections, as written, by 4.5 million dollars. It means more people are paying more taxes. The number of people paying more taxes encompasses 99,000 households. If income tax is the fundamental revenue source of the state, then all Montanans should participate in this tax. He pointed out the need to take a close look to see if the taxpayer lost any other deductions besides the federal income tax. Property taxes can be deducted currently. He pointed out the bill specifically mentioned a portion of the retirement income and tip income. He asked why did this occur. He said because these two groups organized and testified. The bill was changed to take care of them, so they won't cause any more problems. How about the other groups, the other 99,000 households who would loose. They are not organized. He asked if this was the way to write income tax legislation, the groups that have the quick notice get taken care of and the rest of the taxpayers don't. He summarized that the bill would be a setback and he urged the committee to table the bill. **{Tape : 1; Side : A; Approx. Time Counter : 17.6 - 26.5}**

Betty Beverly, representing the Montana Senior Citizens, spoke against the bill. She pointed out the need for fairness, especially concerning senior citizens. She said this bill would adversely affect seniors.

Don Judge, AFL-CIO, said this bill created negative impacts on large numbers of taxpayers.

Questions from Committee Members and Responses: SENATOR ELLINGSON asked the sponsor to explain the fiscal implications. Repeal of the termination date of the charitable endowment credit would cost the state ten million dollars a year yet the repeal of credits would be a benefit to the state by \$746,000 a year. He

noted the direct impact on income taxpayers would be to increase their tax liability by about five million dollars a year. **{Tape : 1; Side : A; Approx. Time Counter : 26.5 - 30}**

SENATOR ELLIS presented amendments that would address those concerns regarding the repeal of those credits.

EXHIBIT(tas18a02) The amendments radically changed the fiscal note. He recommended a new fiscal note be considered for the sake of clarification. He passed around a list of tax credits that were removed from the repealer. **EXHIBIT(tas18a03)** **SENATOR ELLINGSON** asked that the committee consider what the tax rates would do just on the income tax filers, whether it would raise revenue or cost revenue to the state.

SENATOR STONINGTON asked about the goal of reducing the marginal tax rate. **Mr. Nordtvedt** replied that the biggest issue in the Montana income tax was the treatment of different categories for married people filing jointly or married people with comparable incomes filing separately. The state needs a thorough debate on how you want to treat these two categories of taxpayers. The biggest movement of tax hits from one group of people to another will be from married couples making significant income who could now file separately, but under the tax reform would not be able to do this. This is the fundamental issue and the heart of the fiscal impact on different taxpayer; why there is 99,000 people with substantial tax increases while more taxpayers will get smaller tax decreases. **{Tape : 1; Side : B; Approx. Time Counter : 2.7 - 12.6}**

SENATOR BOHLINGER said he understood the argument about taking people off the income tax roles as it gave people a sense of ownership in government that they were helping pay for government. The bill was appealing because it would drop off the lowest paid Montanans. **Mr. Nordtvedt** said that he had made this mistake twice. He was concerned that there was a major tax that fewer and fewer people pay. It is important that all taxpayers have some stake in the spending levels of their government, the size of their government and the size of their taxes. **{Tape : 1; Side : B; Approx. Time Counter : 12.6 - 23}**

SENATOR BOHLINGER asked **SENATOR ELLIS** about legislation that would stimulate the economy and create job growth. Tax credits have been a way to accomplish this goal. He wondered if eliminating some of these credits would be counter to economic development. He referred to the list of credits, Exhibit 3, that were programs that had economic development tied to it. **SENATOR ELLIS** replied that was not his attention but it was a result of using Governor Racicot's proposals from the last Session. It wasn't taken off the bill and wasn't caught and was introduced

from that basis. The amendments would reinstate some of those. This committee could take some off as they were of little use.

SENATOR ELLIS referred to **Mr. Nordtvedt's** statement of taking those lower paying taxpayers off the roles. When the exemptions and deductions are increased comparable to federal law, that benefits all the taxpayers on the lower end of the schedules. The tax rate is lower until you get up to \$65,000. Not only was the effective tax rate lowered, but the deductions and exemptions were increased. He stated that was how the bottom half benefitted. The top half benefitted because of simplicity. The intention of the bill was not to take people off the tax roles. The intention of the bill was to make the system simpler and more easily complied with. **EXHIBIT (tas18a04)**

SENATOR BOHLINGER asked how this might change the perception that Montana had a high tax rate and would possibly discourage taxpayers moving to Montana. **SENATOR ELLIS** pointed out that taxpayers try to avoid taxes.

SENATOR STONINGTON asked if there were other options since this bill affected one third of the households in Montana. **SENATOR ELLIS** described other legislation that was being considered. **SENATOR STONINGTON** asked if the committee would be open to tweaking the effective tax rate. The way the bill is written now, incomes of \$500 thousand plus have a same effective tax rate before and after this bill. As you go down in income brackets there is some increases. **SENATOR ELLIS** talked about the benefits of a resource state, such as Wyoming, which pays all their taxes.

Closing by Sponsor: **SENATOR ELLIS** closed. {Tape : 2; Side : A; Approx. Time Counter : 0 - 15}

EXECUTIVE ACTION ON SENATE BILL 2

SENATOR EKEGREN MOVED DO PASS. **SENATOR STONINGTON** commented that Director Alme was new to his position and he was placed in the position of having to defend previous action on the part of the department. She suggested this bill move through the process. She said she felt justified in bringing this individual constituent's problem forward as it reflected how the Department of Revenue dealt with people and that they were incorrect in their assessment of the issue.

SENATOR COLE suggested it was a mistake to identify individual issues, for example some of his constituents wanted him to intervene in a Fish and Game issue, or some one may want a special road put in. **SENATOR EKEGREN** said he did not see the correlation between someone wanting a special road and someone

being abused by the tax policy of the Department of Revenue. He felt the Legislature was here to address these types of policies.

SENATOR ELLINGSON said he was in favor of the bill but the point about being responsive to constituents and thinking about public policy had to be balanced. It is useful that constituents bring problems because it can identify broad public policy that needs to be considered. Then if it is broad public policy, then it is the right thing. Special treatment for an individual is not right. This particular case should be justified by the department as to their policy choice. He noted Director Alme made a good point that it was not good to change policy retroactively. This is simply clarifying policy, which was not being implemented currently by the Department of Revenue. *{Tape : 2; Side : A; Approx. Time Counter : 15 - 23.6}*

SENATOR BOHLINGER said the testimony by **Mr. Sands** had indicated he had filed as a Sub-S Corporation as opposed to a C Corporation, in a timely manner, and as a consequence the earnings of the corporation should flow directly to him and he'd be taxed on those earnings. He said he did not understand the Department's argument for saying this wasn't done, and for some reason they disqualified this election. If an error has been made, if he has been unfairly taxed, then there should be some avenue for correction of those errors, even if it is done through the legislative process. It appears, from the information given to the committee, that he has been taxed unfairly. *{Tape : 2; Side : A; Approx. Time Counter : 22.9 - 25.4}*

SENATOR GLASSER said that retroactivity should be reserved only to correct what the collective body perceived to be wrong.

SENATOR ELLIS pointed out the Department of Revenue had plenty of time to resolve this issue. He felt Section one of the bill needed to be passed in any case. If there was any doubt by the department about how this should be treated, this bill would address it - it is already taxed, there should be a credit applied. He pointed out it was not known what the revenue implications of the bill would be. *{Tape : 2; Side : A; Approx. Time Counter : 25.4 - 30}*

SENATOR ELLIS said it was unknown how many taxpayers this would consider. Retroactively may not be a good idea since it was unknown what the state would be obligated for. **SENATOR STONINGTON** said that her understanding of the Minnesota situation was when the federal government made Chapter S applicable, Minnesota recognized the Chapter S Corporations but elected to continue to tax them at the corporate level because it was their attempt to collect something extra, interest income perhaps, then

Mr. Sands applied that tax and asked for the credit. She pointed out that if he had wanted to work the system, he could have deducted this as corporate income, but he was a Chapter S Corporation in Montana. He went by the rules and applied it as individual income. Because it was a significant amount of money, that is perhaps why it got kicked out of the system. *{Tape : 2; Side : B; Approx. Time Counter : 0 - 3.8}*

SENATOR COLE asked if there was any chance the Department of Revenue could be allowed to come forward and resolve this.

SENATOR STONINGTON said this has been almost a year since she first knew of the situation. She thought it was appropriate to urge the Department to consider this case more carefully. She only brought it to the Revenue and Tax Committee after a final decision by the Department. She asked the Department if they would be willing to go back in to the Office of Dispute Resolution and renegotiate this. She described the resolution hearing that did not give adequate attention to the matter. They had been unprepared. Their brief had been submitted two weeks later and the Department decision was based on the Department's brief. There was no dispute resolution. She described additional steps that were poorly implemented. She stated this was not an expeditious treatment of a good, honest, taxpaying Montana citizen. This a state policy issue. She noted it was the job of the Director to defend the integrity of the Department of Revenue. The Department could not promise anything, as they have the right to preparation for a hearing in front of the State Tax Appeal Board to negotiate a settlement based on the estimation of the risk of loss by the Department. They will defend their position. **SENATOR STONINGTON** recommended the bill be passed and express some legislative intent. If the Legislature leaves this to the Department, the State Tax Appeal Board has already cancelled the hearing because of legislative interest. This has been inadequate treatment by the Department of Revenue and is larger than an individual taxpayer. It is how the Department is treating the citizens of Montana. *{Tape : 2; Side : B; Approx. Time Counter : 3.8 - 10.6}*

SENATOR GLASSER pointed out this issue was considered the price of fairness. He asked what would make people want to come here if we were not fair to the taxpayers of Montana.

CHAIRMAN DEPRATU commented that he had some of the same concerns but did feel this had gone on too long.

The Question was called. The motion **PASSED** 9-0 on a roll call vote.

ADJOURNMENT

Adjournment: 9:20 A.M.

SEN. BOB DEPRATU, Chairman

DEB THOMPSON, Secretary

BD/DT

EXHIBIT (tas18aad)